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No. 93-489

IN THE

Supreme Court of the United States

OCTOBER TERM, 1993

O'MELVENY & MYERS,
Petitioner,
v.

FEDERAL DEPOSIT INSURANCE CORPORATION AS RECEIVER FOR AMERICAN DIVERSIFIED SAVINGS BANK, *et al.*,
Respondents.

On Writ of Certiorari to the United States Court of Appeals for the Ninth Circuit

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BRIEF FOR LEE H. HENKEL III AS *AMICUS CURIAE* IN SUPPORT OF PETITIONER

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QUESTIONS PRESENTED

The petition presents two questions, one of which acts as the analytical steppingstone for consideration of the other:

1. Whether state law provides the relevant substantive standards for evaluating equitable defenses to state-law tort claims made by an insolvent thrift.

2. If state law would govern such defenses in that context, whether, notwithstanding that fact, those defenses must be evaluated under different federal substantive standards when the same tort claims are made not by the thrift but by a federal receiver.

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INTEREST OF THE *AMICUS CURIAE*

This Court granted review in this case in response to the parties' representations that the decision below conflicts with the decision in *FDIC v. Shrader & York*, 991 F.2d 216 (5th Cir. 1993), petition for cert. pending, No. 93-651. *Amicus* Lee H. Henkel III is a respondent in *Shrader & York* and has filed a brief in opposition to the petition for a writ of certiorari in that case. Because the parties, albeit incorrectly, have linked the two cases, Henkel's interest here is manifest. Both parties have consented to the filing of this brief.

ARGUMENT

The parties in this case contend that the decision of the Ninth Circuit below conflicts with that of the Fifth Circuit in *FDIC v. Shrader & York*, 911 F.2d 216 (5th Cir. 1993), petition for cert. pending, No. 93-651. A close comparative analysis of the two cases, therefore, should assist the Court in its consideration of the issues the parties have asked it to decide. This analysis reveals, *inter alia*, that there is in fact no true conflict because the cases present conceptually distinct issues.

In broad outline, of course, the two cases are quite similar. In each case the Federal Deposit Insurance Corporation ("FDIC") has sued a law firm contending that the firm is liable for malpractice in the representation of one or more now-insolvent thrift institutions. In each case the defendant law firm has asserted a defense that might or would have been successful against the thrifts themselves. The thrust of the government's argument in each case is that federal law "protect[s] federal receivers against claims and defenses that might have been successful against the institution." *Shrader & York* Pet. 5. Thus each case can be analytically broken down into two components: (1) would the law firm's defense be good as against the thrift? (2) if so, does it nevertheless fail as against the FDIC?

Although the two cases resemble one another in these general ways, in their particulars they are quite different. To begin with, it is undisputed that in *O'Melveny* the FDIC is acting as the receiver of the insolvent thrift, and the government contends that a receiver represents "the entire community of interests in the corporation—creditors as well as stockholders." *Pepper v. Litton*, 308 U.S. 295, 307 (1939) (describing those to whom a corporate director owes a fiduciary duty). In contrast, it is undisputed that in *Shrader & York* the FDIC is acting not as a receiver but rather as an assignee of the insolvent thrift. *See Shrader & York* Pet. 2 n.1. Thus in *Shrader & York*, as in *FDIC v. Ernst & Young*, 967 F.2d 166, 169 (5th Cir. 1992), "the FDIC's decision to sue only as . . . assignee" rebutted the essential factual predicate on which its legal argument was based.

The government suggests that the distinction between a receiver and an assignee should be disregarded in this context. *See Shrader & York* Pet. 5 n.2. Yet this Court has expressly held that when the federal government acts as an assignee it stands in the assignor's shoes and is subject to the same defenses. *Dietrick v. Standard Surety & Cas. Co.*, 303 U.S. 471, 479-80 (1938). If indeed there is no difference between a receiver and an assignee, it is evident, without the need of any further analysis, that the FDIC is wrong not only in *Shrader & York* but in *O'Melveny* as well.

The two cases also differ significantly in their operative facts and in the nature of the defenses asserted by the respective defendant law firms. In *O'Melveny*, the FDIC claims that the firm committed malpractice by failing to uncover and disclose fraudulent acts by the thrift's insiders. The law firm contends that the insiders' fraudulent acts were attributable to the thrift itself; that the thrift could not recover for a failure to uncover and disclose its own acts; and that the FDIC, acting in the capacity as the thrift's receiver, is subject to the same disability. (The Ninth Circuit characterized this defense as one of equitable estoppel. Whether that characterization is accurate is by no means clear. We adopt it here merely to meet the court's reasoning on its own terms.)

In *Shrader & York*, the FDIC claims that the firm committed malpractice by failing to advise the thrifts that certain commercial transactions required prior regulatory approval. The law firm asserts a limitations defense, contending that the statute of limitations began to run when the thrifts knew or should have known the facts establishing the causes of action; that an insider knew those facts no later than 1985 and that his knowl-

edge was attributable to the thrifts; and that the applicable two-year statute of limitations therefore had run before the thrifts became insolvent in 1988 and their remaining assets and claims were assigned to the FDIC.

In the end, the defendant law firm is right, and the FDIC is wrong, in both of these cases. But the paths of legal reasoning in the two cases necessarily diverge, reflecting the different facts and legal issues that each case presents.

I. STATE LAW PROVIDES THE RELEVANT SUBSTANTIVE STANDARDS FOR EVALUATING DEFENSES TO STATE-LAW TORT CLAIMS MADE BY AN INSOLVENT THRIFT

In considering whether the law firm's defense would have been good as against the thrift, the Ninth Circuit in *O'Melveny* was inattentive to the matter of choice of law. The court began with "the unexceptionable general principle that the perpetrator of a fraud cannot be a victim of that fraud." *O'Melveny* Pet. App. 10a. This meant, as the court understood, that the thrift would have been estopped from suing the law firm for malpractice if the insiders' fraud could be attributed to the thrift. *Id.* The court further understood that, under California law, the insiders' fraud would be attributed to the thrift unless the insiders actually had been acting adversely to the thrift. *Id.* at 11a. But in proceeding to consider whether the facts established such adverseness, the court made no attempt to determine and follow California legal principles and decisional law. Instead, the court fashioned what can only be described as a federal common law rule that has nothing to do with actual adverseness. The court reasoned that "insiders' conduct is . . . not attributable to the corporation if a recovery by a plaintiff would serve the objectives of tort liability by properly compensating the victims of the wrongdoing and deterring future wrongdoing." *Id.* at 12a. Numerous California cases seemingly to the contrary were cited only to be distinguished on their facts. *Id.* at 12a n.7, 13a n.8. Apparently believing

that a recovery by the thrift would have served "the objectives of tort liability," the Ninth Circuit concluded that the insiders' wrongdoing should not be attributed to the thrift and that the thrift itself therefore would not have been vulnerable to a defense of equitable estoppel. *Id.* at 10a.

It is by no means clear that the Ninth Circuit deliberately substituted federal common law in place of California law in considering whether a defense of equitable estoppel would have prevailed against the thrift. Certainly the court did not acknowledge that that was what it was doing. On the other hand, it is plain that the court was not conscientiously applying California law. In contrast, in evaluating the limitations defense in *Shrader & York* the Fifth Circuit carefully applied state law.

Although the acts of alleged malpractice in *Shrader & York* all had occurred during or prior to 1985, suit was not brought until 1991. *Shrader & York* Pet. App. 3a, 26a. The Fifth Circuit noted that "[t]he Texas limitation period for malpractice claims is two years," *id.* at 7a, and that under Texas law "the limitations period on legal malpractice begins to run when 'the claimant discovers or should have discovered through the exercise of reasonable care and diligence the facts establishing the elements of his cause of action.'" *Id.* at 10a, quoting *Willis v. Maverick*, 760 S.W.2d 642, 646 (Tex. 1988). It was undisputed that an insider had contemporaneous knowledge of such facts, and the court noted that in Texas the knowledge of corporate insiders is imputed to the corporation "to determine when the statute of limitations began to run." *Id.* at 12a, citing *Alice Roofing & Sheet Metal Works, Inc. v. Halleman*, 775 S.W.2d 869 (Tex. App. 1989). The court acknowledged that in Texas, as elsewhere, "courts will generally not impute a bank officer or director's knowledge to the bank if the officer or director acts with an interest adverse to the bank." *Id.* at 15a. In order to identify the proper standard of adverseness,

the court expressly looked to Texas decisional law. *Id.* at 16a-17a, discussing *Goldstein v. Union Nat'l Bank*, 213 S.W. 584 (Tex. 1919). Applying that standard, the court determined that (with a single exception not here relevant) the knowledgeable insider had not been acting adversely and his knowledge therefore was attributable to the thrifts. *Id.* at 20a-23a. Accordingly, the Fifth Circuit concluded that the statute of limitaitons had run long before the lawsuit was initiated. *Id.* at 10a. It follows that if the thrifts, rather than the FDIC, had brought suit in 1991, their suit unquestionably would have been barred.

The Fifth Circuit's careful invocation of state law in *Shrader & York* was exemplary. It is beyond serious dispute that state law governs a thrift's claim against a law firm for malpractice. *See Bank of America Nat'l Trust & Savings Ass'n v. Parnell*, 352 U.S. 29, 33-34 (1956). The assertion of such a state-law tort claim in purely private litigation simply does not implicate the sort of "uniquely federal interests," *Texas Industries, Inc. v. Radcliff Materials, Inc.*, 451 U.S. 630, 640 (1981), quoting *Banco Nacional de Cuba v. Sabatino*, 376 U.S. 398, 426 (1964), that on rare occasions have been held to warrant the replacement of state law with judge-made federal common law. *See, e.g., Boyle v. United Technologies Corp.*, 487 U.S. 500 (1988). Indeed, in *O'Melveny* the Solicitor General apparently has conceded, by not arguing the contrary, that state law would govern the viability of the law firm's defense as against the thrift itself. The Solicitor General further appears to recognize, for he does not contend otherwise, that under California law the law firm's defense indeed was good against the thrift.

II. STATE LAW ALSO PROVIDES THE RELEVANT SUBSTANTIVE STANDARDS FOR EVALUATING DEFENSES TO STATE-LAW TORT CLAIMS MADE BY A FEDERAL RECEIVER OF AN INSOLVENT THRIFT

Shifting the focus from the rights of the thrift to those of the FDIC in its capacity as receiver, the Ninth Circuit in *O'Melveny* understood the question to be whether an equitable defense good against the thrift nevertheless would fail against the FDIC. The court concluded, relying in part on *D'Oench, Duhme & Co. v. FDIC*, 315 U.S. 447 (1942), that as a matter of federal common law the FDIC was not tarred by the thrift's wrongdoing. In reaching this result, the court expressly refused to "incorporate state law to provide the federal rule of decision." *O'Melveny* Pet. App. 13a-14a. Instead, the court purported to "establish federal law," *id.* at 14a, based upon its perception that "the equities between a party asserting an equitable defense and a bank are at such variance with the equities between the party and a receiver of the bank that equitable defenses good against the bank should not be available against the receiver." *Id.* at 15a.

The legal setting in *Shrader & York* is very different. The issue there turns on whether, in a suit brought by the FDIC as assignee, federal law supplants a state statute of limitations or otherwise serves to revive stale claims. The rule in this situation is clear: if a claim held by an assignor is time-barred by applicable local law prior to its assignment to the federal government, it remains time-barred in the hands of the United States as assignee. *Guaranty Trust Co. v. United States*, 304 U.S. 126, 141-43 (1938). The federal government acquires by assignment only "whatever rights then survived the running of the statute against" its assignor. *Id.* at 141.

This result was not changed by the Financial Institutions, Reform, Recovery, and Enforcement Act of 1989 ("FIRREA"), Pub. L. 101-73, 103 Stat. 187. Section 11

of the Federal Deposit Insurance Act, 12 U.S.C. § 1821 (d)(14), was amended by FIRREA to read in pertinent part as follows:

> (A) . . . the applicable statute of limitations with regard to any action brought by the [FDIC] as as conservator or receiver shall be—
>
> . . .
>
> (ii) in the case of any tort claim, the longer of—
>
> (I) the 3-year period beginning on the date the claim accrues; or
>
> (II) the period applicable under State law.
>
> (B) . . . the date on which the statute of limitation begins to run on any claim described in . . . subparagraph [(A)] shall be the later of—
>
> (i) the date of the appointment of the [FDIC] as conservator or receiver; or
>
> (ii) the date on which the cause of action accrues.

This provision by its express terms applies only when the FDIC brings suit "as conservator or receiver." It thus has no application to suits brought by the FDIC in the capacity of an assignee. Notwithstanding the enactment of FIRREA, therefore, when the FDIC sues as assignee, as in *Shrader & York*, the rule indisputably remains as stated in *Guaranty Trust*: if the claim was time-barred in the hands of the assignor, it likewise is time-barred in the hands of the federal assignee.

Section 11, as amended, would not have availed the FDIC in *Shrader & York* even if it had been acting, as in *O'Melveny*, as a receiver. This is so for two reasons. *First*, the thrifts' claims in *Shrader & York* all had expired no later than 1987, two years prior to the enactment of FIRREA. It is undisputed that, whatever else it may do, FIRREA does not revive claims that were time-barred

before its enactment. The Fifth Circuit's holding on this issue reflects the rule that "[i]n the absence of a contrary legislative purpose, 'subsequent extensions of a statutory limitation period will not revive a claim previously barred.'" *Village of Bellwood v. Dwivedi*, 895 F.2d 1521, 1527 (7th Cir. 1990), quoting *Davis v. Valley Distributing Co.*, 522 F.2d 827, 830 (9th Cir. 1975). Because no such contrary legislative purpose is expressed in FIRREA, the courts that have considered the matter are unanimous in ruling that FIRREA does not operate retroactively to revive claims that expired before 1989. *See, e.g., FDIC v. Belli*, 981 F.2d 838, 842 (5th Cir. 1993). The Solicitor General quite properly does not challenge this settled construction of the statute in his petition for certiorari in *Shrader & York*.

Second, section 11 could not, in any event, reasonably be construed as reviving *any* claims, including claims (unlike those in *Shrader & York*) that expired after enactment of FIRREA in 1989 but before the FDIC's appointment as an insolvent thrift's conservator or receiver. The effect of section 11 is only to extend the period of limitations with respect to claims that were viable when the FDIC acquired them, in order to provide the FDIC ample time to review the insolvent thrift's affairs and determine a course of action. Section 11 does not revive claims that had expired before the thrift became insolvent. On this point as well, the lower courts, including both the Fifth and Ninth Circuits, are unanimous. *See, e.g., Randolph v. RTC*, 995 F.2d 611, 619 (5th Cir. 1993), petition for cert. pending, No. 93-955; *FDIC v. McSweeney*, 976 F.2d 532, 534 (9th Cir. 1992), *cert. denied*, 113 S. Ct. 2440 (1993).

Before the enactment of FIRREA, the courts properly understood, and stated in numerous cases involving the FDIC, that time-barred claims may not be revived through the legerdemain of federal common law. As the Ninth Circuit explained,

> It is settled law that state limitations statutes are relevant in determining a claim's viability at the time the federal agency acquires the claim. If the state statute of limitations has expired before the government acquires a claim, that claim is not revived by transfer to a federal agency.

FDIC v. Former Officers & Directors of Metro. Bank, 884 F.2d 1304, 1309 n.4 (9th Cir. 1989), *cert. denied*, 496 U.S. 936 (1990). In short, "stale claims may not be revived by transfer to a federal agency." *FDIC v. Regier Carr & Monroe*, 996 F.2d 222, 225 (10th Cir. 1993). *Accord, e.g., FDIC v. Hinkson*, 848 F.2d 432, 434 (3d Cir. 1988).

Clear as this rule was prior to the enactment of FIRREA, it is even more so now. "[O]nce Congress addresses a subject, even a subject previously governed by federal common law, the justification for lawmaking by the federal courts is greatly diminished. Thereafter, the task of the federal court is to interpret and apply statutory law, not create common law." *Northwest Airlines, Inc. v. Transport Workers Union*, 451 U.S. 77, 95 n.34 (1981). It would have been a grave step, and one arguably of dubious constitutionality, if Congress had purported to revive state-law tort claims that had become time-barred under state law. Statutes of limitations "represent a pervasive legislative judgment that it is unjust to fail to put the adversary on notice to defend within a specified period of time and that 'the right to be free of stale claims in time comes to prevail over the right to prosecute them.'" *United States v. Kubrick*, 444 U.S. 111, 117 (1979), quoting *Railroad Telegraphers v. Railway Express Agency*, 321 U.S. 342, 349 (1944). Recognizing this, Congress in FIRREA stopped short of reviving stale claims and acted only to extend the period of limitations with respect to viable claims. Congress having struck this balance, no room is left for judicial imposition of a federal common law rule that would be more invasive and disruptive of state law. *See Halcyon Lines v. Haenn Ship Ceiling & Refitting Corp.*, 342 U.S. 282, 287 (1952) ("because Congress while acting in the field has stopped short of approving the rule . . . here urged, we think it would be inappropriate for us to do so").

D'Oench, Duhme, the case upon which the Ninth Circuit relied in *O'Melveny*, and upon which the Solicitor General relies in *Shrader & York*, obviously does not independently authorize or justify the imposition of a federal common law rule that would revive tort claims that were time-barred by state law prior to their transfer to the FDIC. In *D'Oench, Duhme* and its precursor, *Dietrick v. Greaney*, 309 U.S. 190 (1940), the Court was concerned with the problem created when a bank and the accommodation maker of a note enter into a secret agreement, not reflected on the bank's books, that the note will not be called for payment. The particular agreement in *Greaney* directly violated federal law and thus plainly was unenforceable. *See* 309 U.S. at 198. The agreement in *D'Oench, Duhme* apparently was not itself illegal, but it nonetheless was contrary to "the federal policy evidenced in [the Federal Reserve] Act to protect [the FDIC] from . . . misstatements as to the genuineness or integrity of securities in the portfolios of banks which it insures or to which it makes loans." 315 U.S. at 459. The Court therefore concluded:

> [T]he reach of the rule which prevents an accommodation maker of a note from setting up the defense of no consideration against a bank or its receiver or creditors is not delimited to those instances where he has committed a statutory offense. . . [A]n accommodation maker is not allowed that defense as against the receiver of the bank and its creditors, or at times even as against the bank itself, where his act contravenes a general policy to protect the institution of banking from such secret agreements.

Id. at 458. The rule applied in *D'Oench, Duhme* and *Greaney* is narrow both in its scope and in its rationale. Neither that rule nor any logical extension thereof sanc-

tions disregard of state statutes of limitations. Indeed, the rule of *D'Oench, Duhme* simply has nothing whatever to do with the prosecution of professional malpractice tort claims of the sort asserted by the FDIC in both *O'Melveny* and *Shrader & York*. *See, e.g., Astrup v. Midwest Federal Sav. Bank*, 886 F.2d 1057, 1059 (8th Cir. 1989); *FDIC v. Braemoor Assocs.*, 686 F.2d 550, 554 (7th Cir. 1982), *cert. denied*, 461 U.S. 927 (1983).

It is apparent, moreover, that the Ninth Circuit in *O'Melveny* erred in extrapolating from *D'Oench, Duhme* to a broad rule of federal common law that "equitable defenses good against the bank should not be available against the receiver." *O'Melveny* Pet. App. 15a. The court was mistaken in at least two respects. In the first place, *D'Oench, Duhme* does not contemplate two different substantive rules of law, depending upon the identity of the noteholder. To the contrary, the Court articulated a rule of universal applicability, which protects "a bank *or* its receiver *or* creditors" against enforcement of improper secret agreements. 315 U.S. at 458 (emphasis added). The Court was not overruling the long-standing rule that "the receiver stands no better than the bank." *Rankin v. City Nat'l Bank*, 208 U.S. 541, 546 (1908).

Secondly, the Court clearly did not intend to supplant state law root and branch in all cases brought by or against the FDIC. The rule enforced in *D'Oench, Duhme* and *Greaney* was itself firmly and explicitly rooted in "the policy of the National Banking Act." *D'Oench, Duhme*, 315 U.S. at 458. Absent the overriding authority of such a federal regulatory enactment, settled principles of state commercial and tort law provide a surer and fairer guide to the parties' respective rights and liabilities than does the Ninth Circuit's vague and general prescription that "equity does equity." *O'Melveny* Pet. App. 14a. If indeed federal common law has a role to play in this context, "[t]he presumption that state law should be incorporated into federal common law is particularly strong in areas in which private parties have entered

legal relationships [as in this case] with the expectation that their rights and obligations would be governed by state-law standards." *Kamen v. Kemper Financial Services, Inc.*, 111 S. Ct. 1711, 1717 (1991). The Ninth Circuit therefore erred in refusing to follow "well-established California law," *O'Melveny* Pet. App. 13a, and in "fashioning a federal rule of decision," *id.* at 14a, based upon nothing more than its own general notions of equity.

CONCLUSION

The judgment of the Ninth Circuit should be reversed.

Respectfully submitted,

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